

BEFORE

THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA

DOCKET NOS. 2010-14--19-C

INRE:)
)
BellSouth Telecommunications,)
Incorporated d/b/a/ AT&T Southeast)
d/b/a AT&T South Carolina v.)
Affordable Phone Services, Incorporated)
d/b/a High Tech Communications)
Docket No. 2010-14-C)
)
BellSouth Telecommunications,)
Incorporated d/b/a AT&T Southeast)
d/b/a AT&T South Carolina v. Dialtone)
& More Incorporated)
Docket No. 2010-15-C)
)
BellSouth Telecommunications,)
Incorporated d/b/a AT&T Southeast)
d/b/a AT&T South Carolina v.)
Tennessee Telephone Service, LLC)
d/b/a Freedom Communications USA, LLC)
Docket No. 2010-16-C)
)
BellSouth Telecommunications,)
Incorporated d/b/a AT&T Southeast)
d/b/a AT&T South Carolina v. One Tone)
Telecom, Incorporated)
Docket No. 2010-17-C)
)
BellSouth Telecommunications,)
Incorporated d/b/a AT&T Southeast)
d/b/a AT&T South Carolina v. dPi)
Teleconnect, LLC)
Docket No. 2010-18-C)
)
BellSouth Telecommunications,)
Incorporated d/b/a AT&T Southeast)
d/b/a AT&T South Carolina v. Image Access,)
Incorporated d/b/a New Phone)
Docket No. 2010-19-C)

**RESPONSE OF RESELLERS TO ORS
RECOMMENDATION**

INTRODUCTION

The Office of Regulatory Staff ("ORS") did not participate as a party to this case but observed the proceedings and has reviewed the evidentiary record. Based on that information, ORS filed a letter with the Commission on April 6 in which ORS submitted "recommendations for the Commission's consideration...in this proceeding." The Resellers will not have the opportunity to cross-examine an ORS witness about these recommendations. That is unfortunate. Under cross-examination, the Resellers believe that the strengths and weaknesses of ORS's analysis would become clear. Given the large amounts of money at stake, this case is of critical importance to the Resellers, especially One Tone Telecom, Inc., a small reseller based in Seneca, one of the first competitive carriers in South Carolina and one of the Respondents in this case. Without the ability to cross-examine an ORS witness, the Resellers have to rely on this brief and oral argument to communicate where the Resellers agree with ORS and where, the Resellers respectfully submit, ORS has not fully considered nor understood the Resellers' legal and policy arguments. Without rehashing the points already made in the Resellers' brief and proposed orders, the Resellers submit this response to OSR's letter and reiterate their request for oral argument to discuss these issues further and respond to questions from the Commission.¹

ARGUMENT

A. Cash Back Promotions

First and foremost, both the Resellers and ORS recognize the central issue in this case: when AT&T's retail rate is cheaper than the wholesale rate, AT&T's methodology "could impede a reseller's ability to compete." OSR Letter, at 2.

This situation is not hypothetical. It occurs every time AT&T offers a promotion in which the customer receives a rebate that is more than the retail price of the service. Simply by

¹ If the Commission agrees to hear argument, the Resellers will work with AT&T, as AT&T has requested, to schedule argument as soon as practical.

paying for one month's residential service --- not two, not three, just one --- the customer is entitled to a \$50 rebate, roughly twice the residential rate. In effect, AT&T is paying its retail customer \$25 for agreeing to buy one month's service. When AT&T resells that same promotion to a Reseller, however, AT&T pays the Reseller a credit of only \$22.75.² In other words, the retail rate of (\$25.00) is 15% less than the wholesale rate of (\$22.75). That, of course, is backwards. According to federal and state law, the retail price for residential telephone service should be 15% more, not 15% less, than the wholesale price. AT&T's methodology, as ORS says, "could impede a reseller's ability to compete." That, of course, is an understatement.

ORS has identified the problem. The simplest solution is to follow the recommendation of the Louisiana Commission Staff and make one modification to the AT&T formula. As long as the effective retail rate (the retail price less the rebate) is greater than zero, nothing changes. In that situation, AT&T's methodology results in a retail rate that is 15% higher than the wholesale rate, as it ought to be. But when the effective retail rate is less than zero, AT&T's formula results in a retail rate that is 15% lower than the wholesale rate. As ORS and the Louisiana Staff both found, that result "impede(s) competition." The self-evident solution is to determine the effective retail rate and then deduct, not add, the wholesale discount. For example, when the effective retail rate is (\$25.00), the wholesale price under AT&T's formula is (\$21.25), which is 15% higher than the retail rate. Instead, the wholesale price should be (\$27.75) which is 15% lower than the retail rate. Making that one correction to AT&T's formula insures that the wholesale rate is always less than the retail rate. It does not produce the result advocated by either party; it produces a compromise. But it resolves the concerns raised by ORS and finally puts an end to this multi-year dispute over the calculation of cash back promotions. It does what both sides asked this Commission to do months ago when these cases were filed. It brings

² For simplicity and ease of calculation, the Resellers are using 15% as the wholesale discount in South Carolina. The actual rate is 14.8%.

closure to Phase I of the consolidated cash back disputes and allows the parties to calculate how much is owed under AT&T's "corrected" formula.

While accurately identifying the problem, ORS proposes a solution that, unlike the recommendation of the Louisiana Staff, creates more problems than it solves. ORS recommends that in determining whether AT&T's wholesale rate is more than or less the retail rate, the Commission should look at the cumulative amount that a retail customer and a wholesale customer pay over a period of ninety days. This approach is a bad idea, for several reasons.

First, ORS's approach fails to bring closure to the issue of how these credits should be calculated and would prevent the Commission from deciding that issue as requested by the parties in this Consolidated Phase. Instead, ORS suggests that *each* AT&T promotion be analyzed to decide whether, and by how much, the retail rate is less than the wholesale rate after ninety days. If the retail rate is less than the wholesale rate, ORS says that the Resellers can bring a complaint to the Commission. This approach invites more litigation each time AT&T files a new cash back promotion and perpetuates the very uncertainty regarding the proper calculation of credits that the parties explicitly sought to have the Commission clarify.

Second, ORS's recommendation that the wholesale and retail prices be calculated over ninety days is inconsistent with the stipulated facts filed by the parties. Those stipulations include the terms and conditions of representative examples of cash back promotions offered by AT&T in South Carolina. Not one of those promotions requires the customer to retain service for ninety days. The only time limit mentioned is thirty days. After thirty days, the customer is entitled to apply for the rebate and, if he meets the other criteria, is legally entitled to receive the cash back award. AT&T could, of course, have required a customer to remain with AT&T for ninety days or more in order to receive a rebate. AT&T chose instead a thirty-day period. ORS should follow the terms and conditions of the promotions as spelled out in the stipulated facts and not expand the thirty-day time period to ninety days or more.

AT&T's own words describe the applicable terms of service for these rebate programs. Those words are set forth in the stipulated facts which have been carefully assembled by agreement of the parties in order to focus the Commission on specific issues. The stipulated facts say that the customer is legally entitled to a rebate after a term of service of thirty, not ninety, days. Those are the facts – the only facts – which must guide the Commission's decision on this issue.

Third, ORS's use of a ninety-day time period has no logical basis. It is a number taken from the FCC's rules which define the difference between short term and long term promotions. See 47 C.F.R. § 51.613(a). Here, all of the cash back promotions described in the stipulated facts are "long term" promotions and available for resale at a wholesale discount. There is no dispute about that. The only question presented to the Commission is how to calculate the "wholesale discount" applicable to these long-term promotions. The ninety-day period used by the FCC to distinguish long and short term promotions has no more relevance to this calculation than it does to the 90 degree temperature in Columbia on a warm day in May. The numbers may be the same but they have nothing to do with each other.

Fourth, the promotion must stand or fall based on what happens during, not after, the required term of service. As explained by the FCC, "[t]o preclude the potential for abuse of promotional discounts, any benefit of the promotion must be realized within the time period of the promotion, e.g., no benefit can be realized more than ninety days after the promotional offering is taken by the customer if the promotional offering was for ninety days." FCC First Report and Order, paragraph 951. Here, the term of service is thirty days. Therefore, what happens after two months, three months, or six months is irrelevant.³

³ If the ORS proposal was adopted by the Commission, it would create a new, third category of promotions that are "long term" *i.e.*, more than ninety days, but which can be cancelled by the subscriber after a shorter period. Using the ORS approach, AT&T could charge a retail rate that is a little cheaper than the wholesale rate for the first three months of service and much higher than the wholesale rate for the following months. The customer, of course,

Finally, ORS's analysis of the cash back issue does not address the Reseller's argument that these promotions are actually "rebates" not "discounts." AT&T offers these heavily advertised promotions, knowing that a significant percentage of customers will be induced to buy the service but will never get the rebate. For those customers, the "cash back" promotions are not discounts at all. As Commissioner Fleming asked during the hearing--How does the customer get a discount if he never gets the rebate? The answer, of course, is that he never does.

AT&T's methodology is based on the assumption that these cash back promotions are discounts. They are not. These promotions are rebates and, under federal law, AT&T is required to offer services to wholesale customers "subject to the same conditions" offered to retail customers. See 47 C.F.R. § 51.603(b). That means, quite simply, that retail and wholesale customers are legally entitled to receive the "same" cash rebate if they meet the conditions of AT&T's promotions.

For the Resellers, this "rebate" approach is simply another way of analyzing this case. It produces the same result as recommended by the Resellers' witness Mr. Joe Gillan for calculating the cash back awards. ORS has not addressed the Resellers' alternative proposal that suggests that these promotions are actually rebates, not discounts. If ORS had presented a witness at the hearing, the Resellers could have explored whether ORS agrees or disagrees with this approach. The Resellers look forward to the opportunity to address these matters at oral argument and anticipate that ORS will participate as well.

B. Waiver of Line Connection Change

When an AT&T retail customer orders residential service, he not only may qualify for a cash back rebate but, in virtually all cases, he also qualifies for a waiver of AT&T's line

could and would cancel his service before the rate went up. This kind of pricing scheme (which is no different in effect from the AT&T methodology) is clearly anticompetitive and not at all, one suspects, what ORS intends.

connection fee. That fee is typically around \$40. This "long term" promotion has been offered for years and, therefore, is available to Resellers at the wholesale discount.

AT&T, however, does not offer this promotion for resale at a wholesale discount. AT&T offers the Resellers a rebate of about \$34.00, which is equal to the wholesale cost of the service. So, if the Reseller applies for and receives the rebate, the Reseller ends up paying an effective rate of \$0.00 for the line connection charge, the same price that the retail customer pays. Since both the retail and wholesale customers end up paying the same rate, ORS concludes that AT&T has met its resale obligation.

This analysis is simplistic and wrong. The retail and wholesale prices are not supposed to be equal. The wholesale price is supposed to be less than the retail rate by the amount of the "avoided retail costs." 47 C.F.R. § 51.607. When AT&T sells a product at wholesale rather than retail, AT&T saves those "avoided retail costs," *ie*, sales, advertising, and customer service. The savings are real. Just because the promotional rate is \$0.00 rather than, for example, \$25.00 or, in the case of a cash back promotion (\$25.00), those avoided costs are still "avoided" and must be taken in account in calculating the wholesale rate. The FCC rule is clear: "The wholesale rate than an incumbent LEC may charge...shall equal the [retail] rate...less avoided retail costs." 47 C.F.R. § 51.607. If the retail rate is \$00.00, the wholesale rate must be less than zero. AT&T is not complying with the FCC rule and ORS, unfortunately, does not address that issue.

C. Referral Promotion

A customer may choose to buy AT&T service because of a cash back rebate, because of the waiver of the line connection charge or because, once he becomes an AT&T customer, he can earn a \$50.00 check each time he refers someone else to AT&T. All three of these promotions are offered by AT&T to attract retail customers. The first two promotions are offered for resale; the "Referral" promotion is not.

ORS accepts, without analysis, AT&T's claim that the Referral promotion is a "marketing referral program" not a "telecommunications service" and is therefore not subject to the federal resale requirement. But the "cash back" promotion and the "line connection waiver promotion" are not telecommunications services either. They are both "marketing programs" which offer customers a financial incentive to purchase AT&T's telecommunications service.

As the Fourth Circuit held in *Sanford*, a promotion which provides a financial benefit to an AT&T customer effectively reduces the retail price of AT&T's service and, if it is a "long term" promotion, must be made available to other carriers. There is no legally defensible difference among these three kinds of promotions. Any long-term promotion which reduces the effective retail price of an AT&T service must be offered for resale, whether the promotion is a cash back offer, a waiver of the line connection charge, or a \$50.00 referral payment.

CONCLUSION

The Resellers and ORS agree that AT&T's method of calculating cash back payments may, under certain circumstances, impede competition. Although the Resellers do not agree with the "correction" recommended by the Louisiana Commission Staff, their approach is a more workable and legally defensible solution than the recommendation of ORS. If this Commission is looking for a reasonable compromise that will finally resolve this long running billing dispute, the Louisiana recommendation is a fair answer.

The issues in these consolidated cases are complex and, at this time, no state commission has ruled on them. South Carolina may be the first. The Resellers therefore ask that the Commission schedule oral argument for the parties, including ORS, before making a decision.

Respectfully submitted,

s/John J. Pringle, Jr.

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May 6, 2011

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing has been served by electronic mail service on the following this 6th day of May, 2011:

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